02-20-09

BEFORE THE PUBLIC UTILITIES COMMISSION

OF THE STATE OF HAWAII

- - - - In the Matter of - - - -	)	Docket No. 2008-0274
	)	
PUBLIC UTILITIES COMMISSION	)	
	)	
	)	
Instituting a Proceeding to Investigate Implementing a Decoupling Mechanism for Hawaiian Electric Company, Inc., Hawaii Electric Light Company, Inc. and Maui Electric Company, Limited.	)	

HAWAII RENEWABLE ENERGY ALLIANCE RESPONSE

TO THE APPENDIX 2 QUESTIONS

OF THE

NATIONAL REGULATORY RESEARCH INSTITUTE SCOPING PAPER ON DECOUPLING

AND

CERTIFICATE OF SERVICE

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The Hawaii Renewable Energy Alliance ("HREA") respectfully offers its response, per the Commission's letter dated January 21, 2009, to the questions included in Appendix 2 of the National Regulatory Research Institute's Scoping Paper entitled: *"Decoupling" Utility Profits from Sales: Design Issues and Options for the Hawaii Public Utilities Commission* ("Scoping Paper").

The response, which starts on the next page, is based in large part on HREA's consideration of an alternative decoupling mechanism based on the Idaho Power Fixed Cost Adjustment Decoupling Mechanism Model ("Idaho Model"). Overall, we believe the Idaho Model is straightforward and easy to implement compared to the HECO and CA models.

Appendix 2: Questions for the Parties

1. Why do electric utilities need decoupling at this time? Please address decoupling needs created by the utility's rate design and Hawaii's emphasis on electricity strategies that would reduce utility sales. If possible, quantify the need.

HREA Response:

HREA understands that decoupling is desired by HECO at this time primarily to provide a more dependable revenue stream and earnings, which in turn provide confidence to its shareholders and promotes their overall financial health. Overall financial health helps HECO maintain their bond ratings, which in turn benefit ratepayers by lowering HECO's costs to finance its investments in infrastructure. Decoupling will also help HECO become less concerned about revenue losses, which in part can be caused by increased energy efficiency and other demand reduction measures. Finally, these demand reductions are a key part of the strategy of the Hawaii Clean Energy Initiative ("HCEI") to reach 70% of Hawaii's electricity demand via clean energy by 2030.

1.1. Does the administration of the energy efficiency programs by a third-party administrator affect the need for and potential benefits of decoupling?

HREA Response:

HREA believes decoupling is required whether energy efficiency programs are administered by the utility or third-party administrator. HREA believes those programs administered by the latter will be more cost-efficient and hence more beneficial to ratepayers and the utility.

1.2. Is the need for decoupling the same on each island? Please consider the frequency in curtailments of as-available renewable generation.

HREA Response:

Qualitatively, as HREA has not conducted a detailed analysis of the potential impact of decoupling for each island, we believe there is a need for decoupling on each island.

However, we believe the need will vary in terms of the relative rates that the utility is or will experience in terms of revenue erosion. We believe the revenue erosion will be greater in on the neighbor islands, in part, given their relatively higher rates and higher customer bills per kWh demand.

HREA is confused as to the intent of the request to consider the frequency of curtailments of as-available renewable generation. That said, we are concerned about the potential impact of new renewable generation on existing renewable generation, and especially projects, such as the windfarms on Maui and the Big Island, that are already subject to curtailment. This issue must be addressed as additional renewable generation is added, whether on the customer-side or utility-side. Specifically, HREA supports a policy that there should be "no harm done" to the existing generators, as new generation is added. It is not clear at this point, however, whether such a policy is best implemented in the instant docket or in conjunction with the Feed-In Tariff or the Competitive Bidding Framework.

2. Please propose a preferred decoupling methodology and in doing so, please answer these questions.

HREA Response:

HREA is currently evaluating an alternative decoupling mechanism based on the Idaho Fixed Cost Adjustment Decoupling Mechanism Model ("Idaho Model"), also referred to as a "true-up mechanism" by Idaho Power. Overall, we believe the Idaho Model is straightforward and easy to implement compared to the HECO and CA models. The Idaho Model does include a revenue adjustment mechanism, based on an average annual revenue requirement increase, which is "trued-up" annually. The following criteria on which the Idaho Model was developed and implemented by Idaho Power[1]:

[1] Idaho Public Utilities Commission, Case No. IPC-E_04-15, Order No. 30267, dated March 12, 2007.

1. *"Stakeholders are better off than they would have been without the mechanism,*
2. *Cross-subsidies are minimized across customer classes,*
3. *Financial disincentives are removed,*
4. *The acquisition of cost-effective DSM is optimized,*
5. *Rate stability is promoted,*
6. *The mechanism is simple,*
7. *Administrative costs and impacts of the mechanism are known, manageable, and not subject to unexpected fluctuation,*
8. *Short and long term effects to customers and company are monitored,*
9. *Perverse incentives are avoided, and*
10. *A close link between the mechanism and desired DSM outcomes is established.*

We will have more to say about our decoupling mechanism proposal in our statement of position.

2.1. Should the decoupling process decouple the utility's earnings (or revenues) from the effects of changes in weather, economic upturns/downturns, taxes, costs of financing, the utility's credit rating or other external variables? How are the sales impacts of efficiency programs segregated from these factors, and how does the commission monitor these factors going forward?

HREA Response:

HREA believes the decoupling process will likely include all the "effects" noted in the question, as it would be quite difficult to "sort out" the effects of each, and furthermore, it would be difficult to establish which effects were attributable to the utility's actions.

Regarding the impacts of "efficiency" programs from the other factors, HREA would agree that HECO has done a good job of tracking efficiency impacts to date, including all of the ongoing DSM programs and some elements that preceded utility DSM in Hawaii, such as the installation of solar water heaters and certain distributed renewable generators.

2.2. Does decoupling that ensures a utility's earnings associated with lost sales create a disincentive for utilities to manage these costs effectively or to invest in capital projects rather than purchase energy or other services?

HREA Response:

No. HREA does agree that a good outcome from decoupling would be increased "energy efficiency" whether facilitated by HECO or the Public Benefits Fund Administrator. Consequently, HREA believes the progress on energy efficiency and other demand reductions should be monitored closely. In doing so and in large part, this would help defer the need for investment in capital projects for new generation and to a degree, purchase energy and other services. For now and moving forward, HREA recognizes that this will be one of the pivotal issues in decoupling and other matters related to the achievement of the HCEI goals.

2.3. Does it eliminate the utility's bias against reduced sales?

HREA Response:

No or not exactly. HREA is not convinced yet that the Idaho Model, or any other decoupling mechanism, will eliminate the utility's bias against reduced sales. We do believe decoupling can "reduce" the utility's bias against "reduced" sales.

2.4. Does it accurately decouple sales and earnings (i.e., reinstate authorized earnings associated with lost sales)? Please provide supporting examples and calculations that address how lost earnings are calculated.

HREA Response:

No. The Idaho Model is based on decoupling sales from revenues rather than earnings. Note: HREA understands, from the NRRI Decoupling Scoping Paper, that "earnings" refers to "profits" rather than revenues.

2.5. Does it encourage customers to be energy efficient?

HREA Response:

No or at least not by itself. Decoupling must be accompanied by active DSM programs either conducted by the utility, the Public Benefits Fund Administrator and/or energy service providers. And in the absence of all that, increasing costs of electricity have and will continue to encourage customers to be more energy efficient.

2.6. Is it easy to understand?

HREA Response:

Yes. HREA believes the Idaho Model is easy to understand, as it is less complicated than the HECO and CA proposals. We will discuss this more in our SOP.

2.7. Are Hawaii's electric utilities' existing metering and customer service systems adequate to support decoupling? If no, recommend enhancements.

HREA Response:

Yes, and HREA is assuming that the decoupling mechanism would require a new line item on customer bills.

2.8. Is it easy to administer (monitoring, audits, hearings, reconciliation)? Estimate the administrative costs including regulatory costs.

HREA Response:

Yes. An adaptation of the Idaho Model that HREA is consider would incorporate a simple decoupling mechanism based on establishing an initial annual revenue requirement and a baseline annual revenue adjustment to be applied in "Year 1" and subsequent years. For example:

- *The initial annual revenue requirement would be established via the appropriate rate case for each utility;*

- *The initial annual revenue adjustment would be established retrospectively by calculating an 'average revenue requirement adjustment" based on the average revenue requirement increase or decrease over the past 5 to 10 years. The adjustment would be expressed as a percentage (%) increase or decrease;*
- *Moving forward, the "Year 1" annual revenue requirement would simply be the initial annual revenue amount increased by the average annual revenue adjustment, e.g. 3%;*
- *During the first year, revenue balance accounts ("RBAs"), such as proposed by HECO, would be used to establish actual performance compared to the initial annual revenue requirement on a monthly basis;*
- *An annual "true-up" would be conducted, e.g., at the end of each calendar year, by summing all the RBAs and comparing the total with the "Year 1"annual revenue requirement. HREA believes if the "actual revenue requirement" is within a half a percent of the "Year 1" requirement, the balance (positive or negative" would then be carried forward to the next year. If the "actuals" exceeded a half of a percent from the target, the "actual" percentage increase or decrease could be used for "Year 2." We say "could" in this case, as there could be extenuating circumstance whereby arguments could be made for leaving the annual revenue adjustment the same; and*
- *Moving forward, the "Year 2"annual revenue requirement would be the "Year 1" annual revenue requirement increased by the annual revenue adjustment (in this example, 3%), and so forth, in subsequent years. Likewise the monitoring and annual true-up would be conducted in the same manner as for "Year 1."*

HREA believes this approach should be implemented on a pilot basis for 3 to 5 years.

2.9. If the proposed method herein is different from the method proposed by the Agreement, why is it superior?

HREA Response:

HREA's believes the approach above is remarkably more simple than those provided by HECO and the CA, and we believe will be functionally and equitably superior.

3. What actions, if any, are required to identify with accuracy each utility's fixed and variable costs?

HREA Response:

All costs (fixed, variable, marginal, embedded) are calculated in total and for each rate class in rate cases before the Commission. So, as noted above in our response to 2.8, the appropriate rate case would be selected to initial the decoupling mechanism.

3.1. What fixed charges are recovered through the utility's volumetric rates by rate component?

HREA Response:

HREA is not an expert in this area. However, we understand that it is a common utility practice to recover a portion of fixed charges via the volumetric (or variable) rates. While it may make sense to redesign the rate structure so that all fixed charges are paid for by customer per the fixed rate portion of his bill, redesigning the rate structure to do so may be problematic at this time in Hawaii. Moreover, we believe the proposal outline above in our response to question 2.8, does not require any changes to rate design.

3.2. Is the information needed to allocate costs into fixed and variable costs included in a current rate filing? If yes, please provide.

HREA Response:

Yes. HREA understands that the information needed to allocate costs are included in all utility rate cases in Hawaii. HREA believes HECO and the CA are in a better position to provide such data, as HREA does not archive that information.

3.3. How should the Commission differentiate between fixed and variable costs?

HREA Response:

Again, we understand this information is available from rate cases. However, as noted above in our response to question 2.8, HREA's proposed decoupling mechanism is based on total revenues. So, to the extent that detailed fixed and variable cost are relevant to rate cases, they would be relevant to the Idaho model.

3.3.1. What timeframe should the Commission consider in setting fixed and variable costs?

HREA Response:

HREA is not an expert in this area. However, we understand that rate cases are generally conducted every three years for each utility. Given that, a three year timeframe would appear to be appropriate.

3.3.2. Are some "fixed costs" simply long-run variable costs that appear fixed in the short term and how should this affect decoupling?

HREA Response:

HREA does not have a response to this question.

3.4. To what extent, if any, should the Energy Cost Adjustment Clause (ECAC) be modified if decoupling is enacted? Are any fixed costs recovered via the ECAC, and if so, should they be removed? To what extent should performance incentives inherent in the clause be modified or removed in order to remove the connection between utility sales and earnings? Should these incentives instead be recovered through the other charges?

HREA Response:

HREA believes the ECAC would not need to be modified to be integrated with the Idaho Model. We understand that no utility fixed costs are recovered via the ECAC. Instead, we understand the ECAC is both a fuel-price adjustment for the utility's generators, and the mechanism for recovering the cost of purchased power from independent power producers, including renewable generators and co-generators.

The question regarding performance incentives in ECAC is a good, but gnarly one. As renewable advocates, HREA has always felt that the ECAC provided the utility with a disincentive for investing in and/or purchasing renewable power. However, now with our Renewable Portfolio Standards law, the aggressive HCEI goals, potential Climate Change Actions and a Hawaii adaptation of the Idaho Model, the disincentive of the ECAC will be softened. That said, HREA does not have any proposals for modifying ECAC at this time.

4. What level of specificity is required on a customer's bill to support a decoupling adjustment (e.g., if allocated by rate component, should there be a line item for each part of the decoupling adjustment on the bill)?

HREA Response:

HREA believes that only a simple line item showing the monthly deviation from the annual revenue requirement is needed. Of course, there could also be a summary explanation of the decoupling mechanism and a link to the Commission's web-site for a detailed explanation of decoupling.

5. Do all customers share in the benefits of improved energy efficiency, or only those customers who improve their own energy efficiency?

HREA Response:

HREA believes that all customers will share in improved energy efficiency. Clearly, those that improve their own energy efficiency will benefit directly and to a larger degree than other customers. Over time, all customers will benefit from energy efficiency due to the avoided fuel costs, deferral of new generation and T&D investments, lowered greenhouse gas emissions and overall economic stimulus that energy efficiency can provide. Finally, HREA believes that appropriately designed and implemented energy efficiency and other demand reduction measures will result in rate reductions over time.

5.1. What does the allocation of benefits indicate about the allocation of decoupling's earnings adjustments?

HREA Response:

HREA's initial response is that the benefits should accrue to all rate classes and customers. However, that implies that the benefits should be based on the ratio of fixed costs that each rate class bears directly. This requires further study and consideration, and we reserve the right to comment again at a later time.

5.2. How should the Commission consider each utility's capacity and energy availability in determining the allocation of the decoupling adjustment?

HREA Response:

See our response to the question above.

5.3. Please propose and discuss an allocation methodology for the decoupling methodology proposed at question 2, above. Include responses to the following questions.

HREA Response:

HREA is not prepare to respond to this question at this time or in detail to the following seven component questions, as further study of the Idaho Model and its adaptation to Hawaii is required.

5.3.1. How much of the anticipated change in sales is driven by utility-sponsored programs? Are the programs available to all classes of customers? How are these costs allocated?

HREA Response:

HREA believes that these questions are relevant to good DSM program design, which is at a crossroads n Hawaii. Specifically, it remains to be seen as to which DSM programs are to be administered directly by the Public Benefits Fund Administrator, HECO and other Parties. However, the net result of these programs and their impact on sales and their related will be addressed directly by the adaptation of the Idaho Model, and we believe the causes of lost sales are not relevant.

5.3.2. Can the utilities' net metering protocols allow behind-the-meter renewable energy to be tracked as a distinct cause of lost sales?

HREA Response:

HREA believes this could be done with advanced ("smart") meters. However, HREA if "lost sales" are to be tracked, demand reduction whether from energy efficiency, use of off-set renewable technologies or customer generation, should be distinguished from other causes of "lost sales," e.g., weather effects, general economic cycle downturns, etc.

5.3.3. Does customer growth or attrition mask or exaggerate actual energy efficiency trends?

HREA Response:

No.

5.3.4. Aside from utility-sponsored programs, do all classes of customers have the same cost-effective opportunities for energy efficiency improvements?

HREA Response:

No. HREA believes that large users can effect more efficiency improvements in their operations and they should be incentivized to do so by reduced energy costs or reimbursement through DSM programs.

5.3.5. Can and should the decoupling charge be allocated to promote specific energy efficiency goals such as cutting peak demand or reducing carbon emissions?

HREA Response:

HREA is not sure, but clearly these goals can be accomplished by appropriate DSM program design by the Public Benefits Fund Administrator.

5.3.6. Does energy efficiency offer greater benefits to the economy in one sector than in another?

HREA Response:

Yes. And HREA believes this will become clearer as our DSM programs are expanded by the Public Benefits Fund Administrator.

5.3.7. The utilities contend that some rate classes produce higher rates of return than others do. To the extent that these differences exist, how should they be addressed under the proposed decoupling process?

HREA Response:

HREA believes this issue would not be addressed directly by the Idaho Model.

6. Should the Commission allow the full recovery of lost earnings though the decoupling adjustment or only some percentage of the calculated lost earnings? How much of the risk associated with a change in sales should remain with the utility?

HREA Response:

Clearly, if the Commission allows full recovery of lost earnings, this will shift all the risks for lost sales to the customer. Moreover, this would be one of the key benefits of decoupling to the utility via the Idaho Model (as well as others). The utility would be made whole in a timelier, on-going manner, whereas without decoupling the utility would be filing more frequent rate cases. Either way, the customer pays the bill, and perhaps it could become palatable to the customer to the extent that "he will pay now rather than later."

6.1. If there is a deviation from 100% recovery, should the deviation be symmetric? For example if sales decrease, does the utility receive 75% of the calculated lost earnings but when sales increase, customers get 100% of the adjustment?

HREA Response:

HREA believes the Idaho Model will provide symmetric recovery.

6.2. How does a partial adjustment help meet the goals of the Clean Energy Initiative?

HREA Response:

HREA would not believe that would be the case.

7. How much, if any, of a rate-of-return adjustment is commensurate with the greater certainty in earnings provided by decoupling?

HREA Response:

HREA considers a reduced rate-of-return to be consistent with reduced risk, as would occur with greater certainty in earnings provided by decoupling. However, HREA is not prepared at this time to make any specific recommendations.

7.1. To the extent that decoupling results in less financial risk for the utility, how should the commission quantify that effect and how should this be flowed through to the utility's rate of return?

HREA Response:

See our response to question 7 above.

7.2. Please quantify decoupling's effect on the utilities' "beta" (a measurement of risk) and what that means to the utility's return and ability to move to a capital structure with more debt.

HREA Response:

See our response to question 7 above.

7.3. Can input from the rating agencies be included during development of the decoupling process?

HREA Response:

HREA considers this to be an interesting question, for which we currently have no answer.

8. Some customers may not have the same opportunity to conserve electricity as other customers because differences such as income, access to capital, age, and renting versus owning. How should decoupling adjustments be structured to address this lesser ability to conserve?

HREA Response:

HREA believes these types of equity questions are not addressed by the Idaho Model (and probably not by other decoupling mechanism). We do believe equity issues could potentially be addressed via appropriate DSM program design and implementation.

9. Please propose a customer education program for the decoupling mechanism proposed at question 2 and the allocation methodology proposed at 5.2.

HREA Response:

HREA is not in a position to propose a customer education program for the Idaho Model at this time.

10. To the extent that the decoupling mechanism is intended to help reduce energy consumption, can this adversely affect the state's efforts to incorporate more as-available renewable energy into the grid? Can reduced consumption cause more instances where as-available energy must be curtailed due to the utility's system constraints?

HREA Response:

Our current state goals are not simply to incorporate more as-available (and firm) renewables, but are to increase our use of our indigenous resources, which include both energy efficiency and renewables in support of our current RPS and the broader-based HCEI goals.

HREA supports the following broader-based strategy for demand reductions in support of the HCEI, and more specifically to help customers reduce their bills: (i) increased energy efficiency; (ii) increase use of off-set renewable technologies, such as solar water heating, sea water air conditioning and solar air conditioning, and (iii) customer-sited renewable energy generators, such as PV and wind energy systems. To be clear, while customers can reduce the electric bills by incorporating energy efficiency measures, they will still have energy needs, which can be met with a combination of off-set and net-metered renewables.

HREA also recognizes that reduced consumption can result in curtailment in as-available renewables such as wind and solar. In fact, this is already happening on Maui and the Big Island, especially during night-time low load periods. There are a number of strategies that can be employed to mitigate these potential impacts. For example, HREA believes that the utility should reduce its baseload (or "must-run") capacity to allow for load following generators that can fill in where the as-available renewable energy projects are not producing. By reducing the "must run" facilities in favor of utility

owned or IPP dispatchable projects, more capacity is available for renewable projects on the system and the load following will produce power more efficiently than the older less efficient units currently in the system. See also our response to question 1.2.

11. Do the rate changes associated with the decoupling mechanism merit a new rate case for HECO pursuant to Hawaii Revised Statutes, Chapter 269, or can the changes be accomplished within the scope of the existing HECO rate case? Are public hearings needed, considering the extent of the expected rate changes?

HREA Response:

HREA does not take a position at this time on these questions.

12. Various provisions of the HCEI propose utility surcharges, where the utility will fairly immediately recover its costs (potentially both fixed and variable) through a surcharge that is separate from the normal rates. How can the commission effectively decouple this aspect of the utility rates? Do these surcharges impact the effectiveness of the efforts to decouple rates from earning?

HREA Response:

HREA is not an expert in this area, but believes that any utility surcharge associated with decoupling, such as discussed with respect to the Idaho Model, can be handled readily.

12.1 Please provide details of changes that need to be made to the various HCEI proposals that have already been filed as a result of decoupling.

HREA Response:

HREA is not aware of any changes that need to be made to the various HCEI proposals that have already been filed, as a result of decoupling.

DATED: February 20, 2009, Honolulu, Hawaii

President, HREA

CERTIFICATE OF SERVICE

I hereby certify that I have this day served the foregoing HREA Comments on the NRRI Scoping Paper upon the following parties by hand-delivery and electronic service as follows:

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